

A VALEDICTORY SPEECH BY CHIEF (DR.) J. O. SANUSI,
GOVERNOR, CENTRAL BANK OF NIGERIA,
AT THE EXTRA-ORDINARY MEETING OF THE
BANKERS' COMMITTEE, MAY 25, 2004.

The President, the Chartered Institute of
Bankers of Nigeria
My Colleagues from the CBN and CIBN,
The Chief Executive Officers of Banks and
Other Financial Institutions,
Distinguished Ladies and Gentlemen.

I feel greatly honoured to address you on this auspicious occasion, marking my exit from the Central Bank of Nigeria as Governor and Chairman of the Bankers' Committee. Let me use this opportunity to join you all in welcoming Mr. S. E. Kolawole as the new CIBN President, and bidding Mazi O.C.K. Unegbu farewell and congratulate him on the successful completion of his tenure as CIBN President.

2. You may recall that barely five years ago in this same auditorium, I had the privilege of making an inaugural speech as the incoming Chairman of this Committee when I outlined my vision for the financial system and called for your cooperation. I should, therefore, begin this address by expressing my profound and sincere appreciation to all members for the support and cooperation given to me during my tenure.

3. Ladies and Gentlemen, on my assumption of office as the CBN Governor and Chairman of this important Committee in 1999, I emphasized that we had a joint responsibility not only for the promotion of a sound, efficient and stable financial system, but also the revitalization of our ailing economy towards the path of sustainable growth and development. This occasion provides a unique opportunity to assess our performance, during the past five years in, meeting those laudable objectives.

4. Despite some encouraging developments, particularly the inflation rate, albeit induced by the lull and inactivity in the economy when this

management team assumed duty in June 1999, there were serious institutional problems that continued to render efficient management of the Nigerian economy very difficult. In particular, the financial sector was beset with problems that were capable of precipitating generalized distress and loss of public confidence in the system, increasing the inefficiency of the payments system, and aggravating the problem of excess liquidity in the banking system.

5. Recognising the central role of the financial sector, particularly the banking system, in a market economy, I underlined the urgent need for embarking on financial sector reform as well as the imperative of promoting the efficiency, soundness and stability of the banking system, without which the conduct of effective monetary policy would be impossible.

6. Against the background of my exhortation, I would like to acknowledge, with profound gratitude, the invaluable contributions of this august Committee to whatever may be ascribed as our achievements. As a matter of deliberate policy, the Bankers' Committee was deeply involved in the policy making process, through regular consultations, open-house discussions and regular submission of memoranda on major monetary and financial policy issues before final decisions which, of course, our responsibility and prerogative.

7. In pursuit of our reform agenda, my management team, at its inception, took bold initiatives to restructure and re-engineer the CBN operations and processes with renewed commitment and focus on prompt and efficient service delivery to major stakeholders to promote economic efficiency, growth and development. The implementation of the restructuring/re-engineering programme, code-named Project EAGLES, has been sustained over the period, with tremendous success. Now in the third and final stage of its implementation, we have realized a number of successes, which have enhanced our efficiency and effectiveness in the discharge of our mandate.

Price and Exchange Rate Stability

8. Despite the constraints imposed on the effective conduct of monetary policy, by fiscal dominance and a glut of other exogenous factors, relative price and exchange rate stability has generally been maintained over the review period. We relied on the leverage provided by the instrument

autonomy granted the Bank in 1998 in taking prompt and courageous policy decisions to deal with critical challenges to macroeconomic management. You may recall that, in February 2001, I drew public attention to the likely adverse macroeconomic consequences of the State and Local Governments' reluctance to heed my warning against the immediate use of their shares of the Excess Crude Reserve Account, stressing the importance of macroeconomic stability and the need to save for the rainy day and recognize the limit of the absorptive capacity of the economy. As predicted, the draw-down of the account resulted in excessive growth of money supply, which fueled the inflation rate to double digits and substantial depreciation of the naira.

9. The consequent sustained tightening of monetary policy that involved the issuance of CBN's own intervention security (CBN Certificate) in 2001, among other measures, succeeded in subduing inflation to an acceptable level until its resurgence in September, 2003. Also, the Dutch Auction System of exchange rate determination was re-introduced in July 2002 to achieve a realistic exchange rate of the naira and reduce the persistent demand pressure on the foreign exchange market. The effect was salutary in enhancing the allocative efficiency of the foreign exchange market and in reducing the unacceptably wide arbitrage premium between the official and bureaux-de-change/parallel market exchange rates from over 21 percent in May 2001 to less than 5 percent, currently. The DAS policy is constantly being reviewed to ensure its continued relevance.

Ensuring Banking Soundness

10. Realizing that the soundness and stability of the financial system depend largely on the efficiency and effectiveness of the supervisory process, the regulatory framework and supervisory capacity of the CBN were strengthened to enhance the effectiveness of the Bank's surveillance activities. In the process, the operating licenses of a few terminally distressed banks were withdrawn, while penalties, including suspension from foreign exchange dealership were imposed on a number of other banks that were found guilty of foreign exchange malpractices and unethical behaviour.

11. Following the adoption of universal banking system in 2000, the CBN redefined banking business in Nigeria and granted uniform licence to all banking institutions. Thus, the distinction between commercial and

merchant banks was removed and banks became free to undertake, in addition to traditional banking, capital market activities and insurance marketing services directly or through subsidiaries. This act unleashed the latent capacity and potentials of some banks, which up to that point had operated as merchant banks. Consequently, they grew rapidly, thus enhancing the competitiveness of the banking industry. With the adoption of universal banking, however, the CBN faced new regulatory and supervisory challenges that required capacity building in the areas of both manpower and infrastructural development, which are being effectively addressed.

12. Cognizant of the need to protect the central role of the banking system and guard against the negative externalities associated with bank failures, especially when such failures become wide-spread, the CBN introduced various safeguards to foster good internal governance and protect the banking system. Accordingly, the framework on Contingency Planning for Banking System Crisis for the Nigerian banking system was adopted in 2002, in line with best practices in other jurisdictions for the prevention, management and containment of banking system crisis. Its implementation would enable the supervisory authorities to reduce the incidence of systemic distress through the sharpening of supervisory processes, including self-regulation among the banks and lowering the cost of crisis resolution by ensuring that liquidation comes only as the ultimate resolution option for a bank that is terminally distressed and, more importantly, that when the ultimate option becomes inevitable that the CBN acts decisively to protect the interest of the depositors and stop possible contagion.

13. The Sub-committee of the Bankers' Committee on Ethics and Professionalism was set up in 2001 to address the problem of unethical and unprofessional practices that had become the bane of the Nigerian banking industry. The issuing of Code of Ethics and Professionalism in the Banking and Financial Services Industry by the Sub-Committee was a demonstration of the priority attention that has been accorded to the sanitization of the banking industry. The Sub-committee has been doing a wonderful job and I must specifically thank the members for their immeasurable contribution.

14. Recognizing that there is no single factor that contributes more to institutional failure than the lack of good corporate governance the CBN has, in recent times, placed increased emphasis on the enthronement of good corporate governance in the financial sector. A corporate governance code

has consequently been issued to ensure the establishment of good corporate governance.

15. Despite these initiatives, the CBN efforts toward ensuring a safe, sound and stable banking system are constrained by legal and institutional rigidities. For example, a few banks that are good candidates for merger/acquisition or outright liquidation cannot be decisively dealt with because the legal and institutional frameworks for such actions are weak and porous. In particular, revocation of licence had triggered protracted law suits that virtually frustrated the regulatory efforts of the CBN to effectively protect the interest of the depositors. The best practices in most other countries is that failing banks are made to exit the system before their capital is completely eroded and before they could infest other banks with distress. Ideally, when a bank becomes severely under-capitalized, the regulatory authorities should initiate its early, orderly and efficient exit before the health of other banks, that are otherwise sound, could be jeopardized. Only by so doing can the regulatory authorities, in case of ultimate failure, minimize the loss of bank creditors, sustain depositors' confidence in the system, reduce claims on deposit insurance and maintain the soundness of the banking system as a whole.

16. We, of course, know that the supervisory authorities cannot single-handedly do all these. The Government needs to put in place proper banking and financial legislation that empowers the supervisory authorities to enforce prudential regulations. The establishment of the EFCC is in the right direction and we hope for effective performance of its functions.

Enhancing the Efficiency of the Payments System

17. Towards enhancing the efficiency of our payments system, the CBN embarked on currency restructuring, involving the introduction of higher currency denomination, comprising ₦100 note in December 1999, ₦200 note in November 2000 and ₦500 note in April, 2001. Arrangements for the coinage of ₦5 and ₦10 notes and the introduction of ₦1000 notes, already approved by government, are at an advanced stage of implementation. The restructuring has helped to reduce the volume of currency in circulation and thereby substantially moderate the cost of currency issue and administration. The adoption of automated cheque clearing system, which has facilitated a

considerable reduction in the number of clearing days represents another concrete action towards enhancing the efficiency of banking operations and the payments system.

18. Lately, the CBN Head Office has been linked to its Branch Offices electronically to facilitate real time inter-bank settlements. Also, a new clearing and settlement system became operational on April 1, 2004. The new scheme is designed to further enhance the efficiency of cheque clearing system in the country. The settlement system has seven settlement banks, approved to undertake the clearing of payments instruments, including cheques for the other banks, known as non-settlement banks. This should eliminate the incidence of incessant and unbridled banks' over-drawn account with the CBN for clearing purposes, and allow the CBN to truly play the role of lender of last resort. The reform of the payments system is on-going. Already, the guidelines for the introduction of e-banking that will encourage the use of electronic payments instrument are being issued.

Development Function

19. Without compromising the pursuit of its primary mandate to maintain price and exchange rate stability, the CBN has supported various initiatives designed to strengthen the growth performance of the economy and promote the diversification of its productive base. Specifically, the following schemes were adopted to facilitate development financing in the country:

(i) Agricultural Credit Guarantee Scheme Fund (ACGSF)

20. Existing efforts to promote the development of the agricultural sector were further strengthened. In this regard, the ACGSF Fund was raised from ₦100 million in 1998 to ₦1.0 billion in 1999 and further to ₦3.0 billion in 2001, to ensure increased access to bank credit by farmers. To enhance the impact of ACGS on the development of the agricultural sector, the Interest Drawback Programme (IDP) was developed as an interest rate management framework to assist borrowers under the guarantee scheme to reduce their effective borrowing rates without the risk of introducing discriminatory and administrative control of interest rates.

(ii) Small and Medium Industries Equity Investment Scheme (SMIEIS)

21. Under the aegis of the Bankers Committee the Small and Medium Industries Equity Investment Scheme (SMIEIS) was established to promote the development of small and medium scale industries, as an engine of growth and job creation, reminiscent of the experience of many developed countries and economies of South East Asia. Under the Scheme, all deposit money banks in the country agreed to set aside 10 per cent of their profit before tax annually, for equity investment in small and medium industries. The SMIEIS initiative, in addition to providing finance, also facilitates capacity building as banks are expected to identify, develop and package viable industrial projects, in partnership with their enterprising customers.

22. Despite its initial slow take-off and the teething problems, which were not unexpected, satisfactory progress has been made in the implementation of the scheme. As at end-March 2004, a total of ₦22.3 billion had been set aside, of which ₦8.7 billion had been invested in 167 projects by 53 banks. The funds will continue to grow and, as more experience is acquired by both the banks and the entrepreneurs, and infrastructure improves, the rate of utilization will increase. I believe that it is the most successful SME programme so far designed in the country and the momentum should be maintained.

(iii) Baseline Economic Study by Universities

23. In order to facilitate accelerated utilization of the set-aside fund, the CBN commissioned 7 universities in 2003 to undertake baseline economic studies in the six geo-political zones of the country with a view to compiling a compendium of viable potential industrial projects that can easily be accessed by prospective investors in every state of the Federation. Efforts have also been made to encourage State Governors to provide industrial estates/parks and basic economic infrastructure to woo investors and attract their fair shares of the SMIEIS fund. It is my hope and prayer that this scheme will be sustained after my exit.

(iv) Development Finance Institutions

24. Finally, the Bank has participated actively in the restructuring and recapitalizing of the development banks for enhanced effectiveness. The

Bank of Industry and the Nigerian Agricultural and Rural Development have emerged to support industrial and agricultural development in Nigeria, respectively.

(v) Micro Finance Policy

25. The CBN has collaborated with the World Bank to establish Micro Finance Policy and Programme Development Committee (MFPPDC) to work out the modality for the operation of micro finance institutions in Nigeria as well as prepare the legal and the regulatory/supervisory frameworks under which they would operate efficiently. The SMIEIS has a micro component which is 10 per cent of the funds set aside under the scheme. This should serve as a base fund for the MFPPDC.

(v) Revitalising the Community Banks

26. The community banking scheme is a laudable initiative aimed at redressing the lack of adequate and efficient institutional facilities for mobilising savings for productive activities among the less privileged segment of the society. The CBN has, during the past three years, adopted necessary institutional and regulatory framework, including the creation of the Other Financial Institutions Department to regulate and supervise community banks. Moreover, the Bank has also been supporting capacity building in the banks by providing free training programmes for community bank personnel since 2002.

Challenges Facing the Banking Industry

27. As at the end of March 2004, there were 89 banks in operation in Nigeria with total assets amounting to ₦3,032 billion, compared to ₦1,184 billion as at end-December, 1999. Similarly, aggregate deposit liabilities increased to ₦1,722 billion in March 2004 from ₦535 billion as at end-December, 1999.

28. While a number of banks still exhibit symptoms of weaknesses ranging from under capitalization, illiquidity, poor/weak assets quality and earnings, the profitability of the industry increased phenomenally. The shares of the weak banks' assets and deposit liabilities as percentage of the industry's total were 19.16 per cent and 17.61 per cent respectively, while the industry ratio of non-performing credit to total credit was 19.48 per cent.

These ratios are within the target prescribed by the CBN, which is also in accordance with international standards. In other words, the Nigerian banking system is generally sound.

29. Despite the progress, several challenges still face the banking industry, among which are strengthening/consolidating the gains made in banking corporate governance and soundness, the dilemma of protecting the bank depositors and maintaining macroeconomic stability and reducing fiscal dominance.

Corporate Governance

30. Good corporate governance provides for the separation of powers and duties to ensure checks and balances in any corporate entity. The absence of good corporate governance in some banks has led to insider abuse, fraud and forgeries, and poor lending policies. While we have made significant progress in redressing the problem and placing the issue in the front burner, there is need for the Bankers' Committee to sustain its efforts at attaining zero tolerance to all forms of corporate malfeasance.

Capital Deficiency and Illiquidity

31. The importance of capital as a cushion for supporting operations and absorbing unexpected losses cannot be over-emphasized. Apart from a few banks, which have not met the ₦1billion minimum capital requirement prescribed for existing banks, some others have had their capital eroded by losses. There is need to respond positively to CBN initiative for mergers and acquisition so that some of the current weak banks that constitute a threat to systemic stability can be absorbed.

Protecting Bank Depositors

32. Banking, as a business, is a risky endeavour. However, because of the uniqueness of the sector, stringent regulatory and supervisory oversight is normally imposed on operators to ensure the protection of depositors, especially, in case of bank failure. While the Nigerian Deposit Insurance Corporation (NDIC) was established to instill confidence in the banking system and settle depositors in case of bank failure/revocation of banking licence, the CBN has been constrained in the past to the speedy enforcement of various distress resolution options available to the Bank. There are a

number of marginal banks in the system that are good candidates for merger/acquisition or outright liquidation which are overdrawn with the CBN. The CBN could not speedily send them out of clearing for fear of triggering banking system contagion and crisis of confidence. Furthermore, the Bank could not liquidate the banks so as to settle the bank depositors in a timely manner because of legal constraints.

33. In this regard, it is my belief that once the regulatory/supervisory authorities are satisfied that the condition of a bank is irredeemable, the CBN should be given the powers to quickly withdraw the bank's operating licence and pay off its depositors without resort to long drawn litigation. There is, therefore, the need to strengthen the CBN Act, among other things, to render the revocation of banking licence a purely administrative matter. Besides, since the Bank is not adverse to due legal process, a time limit should be placed on the quick disposal of cases involving bank liquidation if the need arises. The CBN is in dialogue with relevant authorities and it is hoped that acceptable solution will be found in due course.

Macroeconomic Stability and Fiscal Dominance

34. A major challenge facing the banking industry and the economy as a whole is the problem of maintaining macroeconomic stability – low inflation and interest rates, as well as stable naira exchange rate based on Nigeria's economic fundamentals – in the face of fiscal dominance, poor and low economic productive base and poor infrastructure. To maintain stable macroeconomic environment and grow the economy, government should in the short-term save the windfalls from the excess crude revenue and also direct its expenditure to priority areas such as the provision of infrastructure and strengthening of poverty reduction programmes. The saving is critical not only will it be needed on the rainy day, but also to limit the injection of resources above the absorptive capacity of the economy. In the medium to long term, government should ensure the passage of the Fiscal Responsibility Act which would provide the backbone for the sustenance of macroeconomic stability and wealth creation in Nigeria.

CONCLUSION

35. Distinguished Executives, Ladies and Gentlemen, it has been great working with you as the Chairman of the Bankers' Committee in the past

five years. I thank you most sincerely for the co-operation you gave to me during the period and implore you to extend the same to my successor.

36. More importantly, while I retire physically to my country home, I will in my mind continue to remain part of the Nigerian Banking System.

37. I thank you for your attention and God bless.

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Governor,
Central Bank of Nigeria.**

25th May, 2004.